

BEFORE
THE PUBLIC SERVICE COMMISSION OF
SOUTH CAROLINA
DOCKET NO. 2008-5-G

July 1, 2008

IN RE:)	
)	
Annual Review of Purchased)	
Gas Adjustment and Gas Purchasing)	
Policies of South Carolina Electric &)	SETTLEMENT AGREEMENT
Gas Company)	
)	
_____)	

This Settlement Agreement ("Settlement Agreement") is made by and between the South Carolina Office of Regulatory Staff ("ORS") and South Carolina Electric & Gas Company ("SCE&G" or "the Company") (collectively referred to as the "Parties" or sometimes individually as "Party");

WHEREAS, on February 22, 2008, the Public Service Commission of South Carolina (the "Commission") issued the notice of hearing for the 2008 Annual Review of Purchased Gas Adjustment and Gas Purchasing Policies ("PGA") of SCE&G;

WHEREAS, the purpose of this proceeding is to review matters related to SCE&G's gas purchasing practices and policies, administration of its purchased gas adjustment, and the recovery of its gas costs;

WHEREAS, the period under review in this docket is March 1, 2007 to February 29, 2008 ("Review Period");

WHEREAS, ORS has examined the books and records of SCE&G and conducted inquiries and analyses related to the Company's gas purchasing practices and policies, administration of its purchased gas adjustment, and the recovery of its gas costs;

WHEREAS, ORS determined that during the period under review, SCE&G: a) properly administered the purchased gas adjustment; b) employed prudent gas purchasing practices and policies; c) administered the Industrial Sales Program-Rider ("ISP-R") prudently and reasonably and in accordance with the terms of Order No. 2005-619, adopting the Settlement Agreement entered into in Docket No. 2005-113-G, which authorized that program in its current form; d) except as described in the ORS testimony of Roy H. Barnette in this docket, recovered its gas costs consistent with applicable tariffs and Commission orders;¹ e) conducted and administered its hedging program consistent with the authorization granted in Order No. 2006-679; and, f) was prepared during the review period and is currently prepared to meet its firm customers' projected needs via its future supply and capacity asset plans;

WHEREFORE, the Parties have engaged in discussions and in the spirit of compromise, the Parties hereby stipulate and agree to the following terms and conditions:

1) The Parties agree to stipulate into the record before the Commission this Settlement Agreement. The Parties further agree to stipulate into the record the pre-filed direct testimony of James E. Swan, IV, Martin K. Phalen, Rose Jackson, Harry L. Scruggs, Roy H. Barnette, and Carey M. Flynt and the pre-filed settlement testimony of Rose Jackson included herein as Attachment 1 without cross-examination and that each witness will take the stand to present his or her testimony. With respect to this Settlement Agreement, Rose Jackson is the witness designated to be primarily responsible for providing support for the Settlement Agreement.

¹ As reported in Witness Barnette's prefiled testimony at page 7, line 14 through page 8, line 3, SCE&G inadvertently failed to implement a revised gas tariff filed under its gas cost recovery mechanism for the month of June 2007. The error was not discovered and corrected until after 6 billing cycles had been completed. The error resulted in an underbilling during the month of June 2007 of \$57,174. To adjust for this underbilling, ORS has added the amount of \$57,174 to the Company's overcollection total. SCE&G has agreed to this adjustment.

2) For the purpose of setting the gas cost recovery factors, the Parties accept the use of ORS's cost of gas calculations for the period March 1, 2007 through February 29, 2008 as set forth in ORS Audit Exhibit RHB-1 attached to the testimony of Roy H. Barnette.

3) The Parties agree to maintain the monthly adjustment procedure and notification procedure for the total cost of gas factors as adopted in Commission Docket No. 2006-5-G, Order No. 2006-679.

4) The Parties acknowledge the demand charges included in the total cost of gas factors will continue to be calculated as set forth in Commission Docket No. 2006-5-G, Order No. 2006-679 by distributing such costs among the rate schedules based upon a 50-50 allocation of peak design day demand and annual forecast sales. SCE&G agrees to use the 50-50 allocation of peak design day demand and annual forecast sales for demand charges in any recalculation of total cost of gas factors under this Settlement Agreement. The Parties agree that the allocation factors contained on page 3 in Mr. Scruggs's pre-filed direct testimony (Residential 66.84%; SGS/MGS 29.95%; LGS 3.21%) are appropriate and should be used for cost of gas calculations beginning with the first billing cycle of November 2008.

5) As part of this Settlement Agreement, the Parties agree that SCE&G shall continue to charge and recover carrying costs, if applicable, on the cumulative total over- or under-collection balances in the same method and with the same limitations as set forth in Commission Docket No. 2006-5-G, Order No. 2006-679.

6) The Parties agree with the approximately \$10.5 million in credits distributed to gas residential and small/medium general service customer classes from the Prepaid Municipal Fee Account. Discussion of the Prepaid Municipal Fee Account is set forth in Docket No. 2007-459-E and Order No. 2008-49 as well as the testimony of James E. Swan, IV in this docket.

7) The Parties agree that the hedging program and methodologies approved by Commission Order No. 2006-679 in Docket No. 2006-5-G were conducted and administered

during the Review Period consistent with Order No. 2006-679.² The Parties also agree that SCE&G's approved hedging program is to continue through the next review period with the following modifications:

- a) Reduce the percentage of volumes that may be hedged from up to 50% to up to 25%;
- b) Utilize the dollar cost averaging methodology;
- c) Eliminate the Kase ezHedge™ model and any future associated operating and administrative costs with Kase and Company, Inc. for the use of that model once the current contract expires on September 30, 2008;
- d) Reduce the number of forward months on which hedges may be placed to twelve months;
- e) Use call options instead of fixed price instruments where the premium for any call option purchased will be the lesser of or equal to: 1) 10% of current market price of natural gas for the month being hedged, or 2) the cost of an at-the-money³ call option for the month being hedged; and,
- f) Settle its current outstanding hedge positions which expire beyond the twelve month time period described in subsection d) above by taking corresponding offsetting financial positions in the market if the resulting aggregate settlement in total results in a gain and apply this gain to the gas cost over/under collection account used in the cost of gas calculation factor in the month the settlements occur.

² By way of Order No. 2007-595, dated September 6, 2007, in Docket No. 2007-5-G, the Commission approved the continued use of the authorized hedging program and methodologies.

³ An option is at-the-money if the strike price is the same as the current price of the underlying security on which the option is written. The strike price is the price the option holder must pay to exercise the option.

SCE&G agrees to continue reporting to the Commission and ORS within 30 days following the close of each month the results of the hedging program for the preceding month, which report shall include the hedging transactions closed-out during the month, the additions to or subtractions from the cost of gas resulting from closed-out contracts, the costs of operating the program during the month, and a list of open transactions as of the last day of the month for each succeeding month.

The Parties further agree that SCE&G's hedging program shall continue to be operated independent of and shall be accounted for separate from its purchase of physical gas supply.

8) ORS is charged by law with the duty to represent the public interest of South Carolina pursuant to S.C. Code § 58-4-10(B). S.C. Code § 58-4-10(B)(1) through (3) reads in part as follows:

... 'public interest' means a balancing of the following:

- (1) concerns of the using and consuming public with respect to public utility services, regardless of the class of customer;
- (2) economic development and job attraction and retention in South Carolina; and
- (3) preservation of the financial integrity of the State's public utilities and continued investment in and maintenance of utility facilities so as to provide reliable and high quality utility services.

ORS believes this Settlement Agreement reached among the Parties serves the public interest as defined above.

9) The Parties agree to advocate that the Commission accept and approve this Settlement Agreement in its entirety as a fair, reasonable and full resolution of all issues in the above-captioned proceeding and to take no action inconsistent with its adoption by the Commission. The Parties further agree to cooperate in good faith with one another in recommending to the Commission that this Settlement Agreement be accepted and approved by the Commission. The Parties agree to use reasonable efforts to defend and support any

Commission order issued approving this Settlement Agreement and the terms and conditions contained herein.

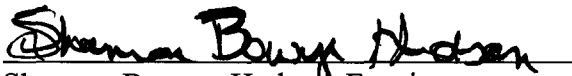
10) The Parties agree that signing this Settlement Agreement will not constrain, inhibit, impair, or prejudice their arguments or positions held in other collateral proceedings, nor will it constitute a precedent or evidence of acceptable practice in future proceedings. If the Commission declines to approve the Settlement Agreement in its entirety, then any Party desiring to do so may withdraw from the Settlement Agreement without penalty or obligation.

11) This Settlement Agreement shall be interpreted according to South Carolina law.

12) The above terms and conditions fully represent the agreement of the Parties hereto. Therefore, each Party acknowledges its consent and agreement to this Settlement Agreement by affixing its signature or by authorizing its counsel to affix his or her signature to this document where indicated below. Counsel's signature represents his or her representation that his or her client has authorized the execution of the agreement. Facsimile signatures and e-mail signatures shall be as effective as original signatures to bind any Party. This document may be signed in counterparts, with the various signature pages combined with the body of the document constituting an original and provable copy of this Settlement Agreement. The Parties agree that in the event any Party should fail to indicate its consent to this Settlement Agreement and the terms contained herein, then this Settlement Agreement shall be null and void and will not be binding on any Party.

WE AGREE:

Representing the South Carolina Office of Regulatory Staff

A handwritten signature in black ink, appearing to read "Shannon Bowyer Hudson", is written over a horizontal line.

Shannon Bowyer Hudson, Esquire

Shealy Boland Reibold, Esquire

South Carolina Office of Regulatory Staff

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WE AGREE:

Representing South Carolina Electric & Gas Company



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1 **SETTLEMENT TESTIMONY OF**
2 **ROSE JACKSON**
3 **ON BEHALF OF**
4 **SOUTH CAROLINA ELECTRIC & GAS COMPANY**
5 **DOCKET NO. 2008-5-G**
6

7 **Q. ARE YOU THE SAME ROSE JACKSON THAT HAS PREFILED DIRECT**
8 **TESTIMONY IN THIS CASE?**

9 **A. Yes, I am.**

10 **Q. WHAT IS THE PURPOSE OF YOUR SETTLEMENT TESTIMONY?**

11 **A. In this settlement testimony, I discuss and support the settlement agreement (the**
12 **“Settlement”), entered into by the parties in this proceeding on July 1, 2008. Specifically,**
13 **I explain the terms of the Settlement as they relate to SCE&G’s gas purchasing practices**
14 **and discuss administration of the hedging program for the period under review.**

15 **Q. PLEASE PROVIDE AN OVERVIEW OF THE SETTLEMENT WITH RESPECT**
16 **TO THE COST OF GAS.**

17 **A. For the period under review, March 1, 2007 through February 29, 2008, the parties**
18 **agreed that SCE&G properly administered the purchased gas adjustment, employed**
19 **prudent gas purchasing practices and policies, administered the Industrial Sales program-**
20 **Rider prudently and reasonably, recovered its gas costs appropriately except for the**
21 **approximately \$57,000 discussed in Roy Barnette’s testimony, and was and is prepared to**
22 **meet the firm demand of its customers. For the purpose of setting the gas cost recovery**
23 **factors, SCE&G accepts ORS’s cost of gas calculations and the Parties agree to maintain**
24 **the monthly adjustment and notification procedure for the total cost of gas factors as**
25 **previously adopted by the Commission. SCE&G Witness Harry Scruggs discusses in his**
26 **testimony and SCE&G and ORS have acknowledged that the calculation of the demand**

1 charges included in the cost of gas factors will continue to be distributed among the rate
2 schedules based upon a 50-50 allocation of peak design day demand and annual forecast
3 sales. Further, the Parties agree that the allocation factors as contained in Mr. Scrugg's
4 pre-filed direct testimony are appropriate and should be used for cost of gas calculations
5 beginning with the first billing cycle of November 2008. SCE&G has also agreed to
6 continue to charge and recover carrying costs in accordance with Commission Order No.
7 2006-679. Finally, ORS and SCE&G agree with the approximately \$10.5 million in
8 credits distributed to gas residential and small/medium general service customer classes
9 from the Prepaid Municipal Fee Account and as discussed in Docket No. 2007-459-E and
10 Order No. 2008-49.

11 **Q. PLEASE EXPLAIN THE SETTLEMENT AGREEMENT WITH RESPECT TO**
12 **THE HEDGING PROGRAM.**

13 **A.** The Parties agree that, during the Review Period, the hedging program was conducted
14 and administered consistent with Order No. 2006-679. The Parties have further agreed
15 that the hedging program should continue through the next review period with certain
16 modifications, which are subject to Commission approval.

17 **Q. WHAT MODIFICATIONS TO THE HEDGING PROGRAM ARE SCE&G AND**
18 **ORS PROPOSING IN THIS PROCEEDING?**

19 **A.** First, the Parties have agreed to reduce the percentage of natural gas volumes which may
20 be hedged from the current level of up to 50% down to a maximum of up to 25% of
21 projected purchases. Second, SCE&G currently uses the Kase ezHedge™ model as well
22 as the dollar cost averaging methodology. The Parties propose that SCE&G eliminate the
23 use of the Kase ezHedge™ model and utilize only the dollar cost averaging methodology

1 on a going forward basis. Once the current contract with Kase and Company, Inc.
2 expires, SCE&G agrees to eliminate any future associated operating and administrative
3 costs related to the Kase ezHedge™ model.

4 **Q. HAVE THE PARTIES AGREED TO ANY CHANGES WITH RESPECT TO THE**
5 **FINANCIAL INSTRUMENTS USED IN THE HEDGING PROGRAM?**

6 **A.** Yes, we have. SCE&G currently operates its hedging program using fixed price
7 instruments. The Parties have agreed to modify the program to exclude the use of fixed
8 price instruments and, alternatively, to use call options where the premium for any call
9 option purchased will be the lesser of or equal to: 1) 10% of the current market price of
10 natural gas for the month being hedged, or 2) the cost of an at-the-money call option for
11 the month being hedged. This modification will reduce the exposure to hedging losses
12 and gains in any one year. Additionally, the Parties have agreed that the program should
13 be modified such that the number of forward months for which the Company may place
14 hedges is reduced to twelve months.

15 **Q. DO THE PARTIES HAVE ANY RECOMMENDATIONS REGARDING THOSE**
16 **OUTSTANDING HEDGE POSITIONS WHICH ARE SCHEDULED TO EXPIRE**
17 **BEYOND TWELVE MONTHS?**

18 **A.** Yes. The Parties have agreed to recommend to the Commission that SCE&G be allowed
19 to settle outstanding hedge positions which are scheduled to expire beyond twelve
20 months by taking corresponding offsetting financial positions in the market, if and only if
21 the resulting aggregate settlement in total results in a gain from the settlements. SCE&G
22 will continue to maintain the original financial positions through their respective
23 expiration dates; however, by settling these positions, SCE&G will establish and “lock

1 in" any aggregate gains in the market on that date. SCE&G will not realize any monetary
2 gain until the dates of expiration of the applicable hedges; however, SCE&G will be able
3 to apply the aggregate gain to the gas cost over/under collection account used in the cost
4 of gas calculation factor in the month the settlements occur. If the Commission approves
5 this request, then the Company would expect to complete the necessary transactions
6 within a reasonable time following its receipt of an Order authorizing the settlements of
7 these outstanding hedges.

8 **Q. HAVE THE PARTIES AGREED TO CONTINUE THE OTHER**
9 **REQUIREMENTS AS PREVIOUSLY SET FORTH BY THE COMMISSION?**

10 **A.** Yes, SCE&G has agreed to continue reporting to the Commission and ORS within 30
11 days following the close of each month the results of the hedging program for the
12 preceding month. Additionally, the Parties have agreed that the hedging program shall
13 continue to be maintained independent of and shall be accounted for separately from its
14 purchase of physical gas supply.

15 **Q. WITH REGARD TO THE SETTLEMENT AGREEMENT, WHAT REQUEST**
16 **DOES THE COMPANY MAKE OF THE COMMISSION?**

17 **A.** The Company respectfully requests that the Commission approve the Settlement
18 Agreement entered by the parties in this proceeding and the findings, terms and
19 conditions contained therein.

20 **Q. DOES THIS CONCLUDE YOUR SETTLEMENT TESTIMONY?**

21 **A.** Yes.

BEFORE
THE PUBLIC SERVICE COMMISSION
OF SOUTH CAROLINA
DOCKET NO. 2008-5-G

IN RE:

Annual Review of Purchased Gas)	
Adjustment and Gas Purchasing Policies of)	CERTIFICATE OF
South Carolina Electric and Gas Company)	SERVICE
)	
)	

This is to certify that I, Pamela J. McMullan, have this date served one (1) copy of the **SETTLEMENT AGREEMENT** in the above-referenced matter to the person(s) named below by causing said copy to be deposited in the United States Postal Service, first class postage prepaid and affixed thereto, and addressed as shown below:

Catherine D. Taylor, Esquire
K. Chad Burgess, Esquire
South Carolina Electric and Gas Company
1426 Main Street, MC 130
Columbia, SC, 29201

Mitchell Willoughby, Esquire
Willoughby & Hoefer, P.A.
Post Office Box 8416
Columbia, SC, 29202



Pamela J. McMullan

July 1, 2008
Columbia, South Carolina